RSC 50-2

JAPAN · ECONOMIC · INSTITUTE

JEI REPORT

A Two-Part Report: A and B

NO. 44B
November 16, 1990

IN THIS ISSUE:

Original Peace Team Bill Dies, New Proposal In The Offing 1

Japan's Current Account Surplus Plummets 3

Japanese Banks Sneeze, World Catches Cold? 5

Diet Calls For Relocation Of Capital 7

Midterm Elections: Few Changes, Japan A Minor Campaign Issue 9

Original Peace Team Bill Dies, New Proposal In The Offing

Representatives of the ruling Liberal Democratic Party and noncommunist opposition parties agreed November 8 to scrap a bill that would have authorized the dispatch overseas of Self-Defense Forces personnel to provide nonmilitary support for United Nations-sponsored peacekeeping activities. LDP secretary general Ichiro Ozawa, one of the most aggressive proponents of including SDF personnel as part of the peace cooperation team, noted, however, that while the original bill was scrapped, both the ruling party and certain members of the opposition parties agreed that it behooves Japan to provide financial and personnel support for U.N.-sponsored peacekeeping missions in the Middle East and other potential hot spots.

Speaking to the press following the withdrawal of the measure, Prime Minister Toshiki Kaifu emphasized that cooperation with the United Nations is necessary for Japan. He stated that he expects "better" (meaning, enactable) legislation will be drawn up through consultations between the LDP and members of the political opposition for consideration during the regular Diet session, scheduled to begin around December 10.

Throughout the three weeks of contentious Diet debate on the proposed U.N. Peace Cooperation Law there was speculation that the LDP secretary general, through his forceful advocacy of the unprecedented foreign policy proposal, in fact was positioning himself to assume the reins of power if Mr. Kaifu was unable to get the bill at least through the LDP-dominated lower house. Judging by the ground swell of opposition to the measure (see JEI Report No. 43B, November 9, 1990), however, Mr. Ozawa may lower his profile or soften his rhetoric since his internationalist approach to foreign policy obviously does not yet mesh with the public's conception of Japan's global role.

What could loosen the prime minister's leadership grip is if the United States and other allies criticize the revised proposal as too watered-down, ineffectual and late in coming. Ruling party elders might then decide that a politically stronger leader would be better able to manage the difficult balance between domestic and international pressures.

Barbara Wanner

Japan's Current Account Surplus Plummets

Japan's most recent balance of payments statistics demonstrate the difficulty of having a cake and eating it too. Certainly the data served up by the Bank of Japan looked appetizing enough: the current account surplus dropped 49.7 percent in the July-September quarter compared to a year earlier (see Table 1). The resulting black-ink entry of $7.5 billion was the smallest since

Table 1: Japan's Balance of Payments

(in millions of dollars)

	Trade Balance	Exports (f.o.b.)	Imports (f.o.b.)	Services (net)	Current Account Balance	Long-Term Capital (net)
1985	$55,986	$174,015	$118,029	$-5,165	$49,169	$-64,542
1986	92,827	205,591	112,764	-4,932	85,845	-131,461
1987	96,386	224,605	128,219	-5,702	87,015	-136,532
1988	95,012	259,765	164,753	-11,263	79,631	-130,930
1989	76,917	269,570	192,653	-15,526	57,157	-89,246
1988: I	21,021	59,345	38,324	-1,337	18,421	-15,142
II	22,448	63,559	41,111	-2,882	18,567	-36,556
III	23,765	65,989	42,224	-3,623	19,052	-42,214
IV	27,778	70,872	43,094	-3,421	23,591	-37,018
1989: I	21,311	66,945	45,634	-3,595	16,064	-5,612
II	19,794	66,560	46,766	-4,892	14,283	-30,801
III	19,770	68,157	48,387	-4,023	14,957	-21,559
IV	16,042	67,908	51,866	-3,016	11,853	-31,274
1990: I	14,393	65,460	51,067	-701	12,305	-16,086
II	13,614	65,510	51,896	-5,279	7,892	-18,985
III(p)	17,267	70,329	53,062	-8,043	7,520	-7,011

Table 2: Japan's Net Purchases of Foreign Securities

(in millions of dollars)

	Bonds			Stocks		
	Purchases	Sales	Net	Purchases	Sales	Net
1985	$291,338	$237,859	$53,479	$5,484	$4,489	$995
1986	1,346,989	1,253,965	93,024	20,917	13,869	7,048
1987	1,273,829	1,200,944	72,885	70,936	54,062	16,874
1988	1,364,061	1,278,249	85,812	76,560	73,567	2,993
1989	1,683,733	1,589,650	94,083	97,056	79,169	17,887
1988: I	332,047	318,877	13,170	18,901	19,467	-566
II	401,293	374,371	26,922	20,518	20,643	-125
III	333,473	307,635	25,838	25,166	23,425	1,741
IV	297,248	277,366	19,882	11,975	10,032	1,943
1989: I	341,774	327,771	14,003	17,724	17,828	-104
II	487,087	461,996	25,091	21,228	15,120	6,108
III	463,493	437,622	25,871	23,602	18,807	4,795
IV	391,379	362,261	29,118	34,502	27,414	7,088
1990: I	356,393	355,524	869	27,640	22,694	4,946
II	350,993	341,640	9,353	19,972	17,819	2,153
III(p)	331,100	320,195	10,905	18,121	17,662	459

1983 for the third quarter and only half as large as the respected Nomura Research Institute had predicted mere days earlier. Coming on top of an equally good move toward balance in the previous quarter, the resultant double-layered treat could well foretell a 1990 surplus of under $40 billion.

Some Japanese analysts worried, however, that the latest data would leave American critics with a bad taste in their mouth. The trade balance -- the single most important component of the current account surplus -- declined only modestly, a fact reflected in the customs-clearance trade statistics released earlier (see JEI Report No. 41B, October 26, 1990). As a result, the sharp decline in the current account surplus stemmed from dramatic changes in its other two elements, services and transfer payments. The surging imbalance in services easily outstripped a quarterly record established in the previous three-month period. Transfer payments, usually a few hundred million dollars, leaped to $1.7 billion for the quarter on the strength of a $1.1 billion outflow in September, related primarily to Japanese financial contributions to the U.S.-organized funding mechanism in support of allies in the Persian Gulf. In particular, Japanese analysts worried that Americans and others would find surging tourism, the largest component of services, and financial aid, the most important part of transfers, less than ideal ways to shrink Japan's external imbalance.

The decline in Japan's current account surplus highlighted another problem from the U.S. perspective. As Japan's sales and purchases abroad move closer to balance, Japanese investors supply a proportionately lower amount to world capital markets. Japan's third quarter long-term capital outflow of $7

billion, a net figure that includes direct and portfolio investment, was only one-third as large as the comparable figure in 1989.

The drop in the net capital outflow resulted primarily from Japanese institutional investors becoming more cautious about additions to their overseas financial holdings. While net bond purchases in the July-September period were the largest during any quarter this year, they still were less than half the size for the same time a year earlier (see Table 2). Net stock purchases have showed an even sharper falloff this year. Since March Japanese investors generally have added to their overseas holdings in months when the Japanese stock market has risen and reduced them when the market fell; the sharpest sell-off occurred in September when investors unloaded $1 billion worth of foreign stocks.

Taken together, the data in Tables 1 and 2 show a consistent, if not altogether reassuring, pattern. The decline in Japan's current account surplus has coincided with a slowdown in the rate at which Japanese institutional investors are supplying world capital markets with funds. With an increasing number of experts believing that U.S. economic growth has slowed dramatically, the data point to a number of dilemmas facing American policymakers. Declining U.S. economic fortunes suggest that tourism or other foreign expenditures would be welcome; the cost, however, would be a decline in the funds that help finance a recession-swelled budget deficit. In short, the Japanese current account statistics point to some of the difficult choices facing U.S. policymakers. As a result, the decline in Japan's surplus is a tempting treat Americans may have a hard time swallowing.

Douglas Ostrom

Japanese Banks Sneeze, World Catches Cold?

After rising to new heights on the back of the domestic economy's long-running expansion, Japanese banks have stumbled as events have transformed some of their strengths into weaknesses. Major Japanese commercial banks now are expecting profit declines for the year ending March 31, 1991 and have had their credit ratings downgraded recently by independent investment services. While the chances of a major bank failure still are remote, Japanese government and private analysts are concerned that the domestic banks' troubles will make it difficult for them to meet international creditworthiness standards. They also question whether the banks' struggles pose a threat to the health of the entire economy. Moreover, the ripple effect could impact the global economy because of the important role Japanese banks have come to play in world finances.

The banks' woes are extensions of the weaknesses revealed in their business results for FY 1989 (see JEI Report No. 26B, July 6, 1990). Despite increases in operating revenues, the values of stock portfolios eroded and higher operating costs cut profits. This trend is continuing, according to the results for the first half of FY 1990 recently released by four major Japanese commercial banks. Dai-Ichi Kangyo Bank, Ltd., Mitsui Taiyo Kobe Bank, Ltd., Fuji Bank, Ltd. and Sanwa Bank, Ltd. estimate that operating revenues grew about 20 percent over the six months beginning April 1 but that pretax profits were off 40 to 45 percent from the same period in 1989. Based on these six-month results, the four banks projected operating revenue growth of 10 percent

NOTE

ONLY THE FOLLOWING PAGES OF THIS

PUBLICATION HAVE BEEN FILMED

Cov. 1, STATISTICAL SUPPLE-

MENT (2pgs.)